



COMMONWEALTH OF KENTUCKY
OFFICE OF THE ATTORNEY GENERAL

ANDY BESHEAR
ATTORNEY GENERAL

CAPITOL BUILDING, SUITE 118
700 CAPITOL AVENUE
FRANKFORT, KENTUCKY 40601
(502) 696-5300
FAX: (502) 564-2894

OAG 17-018

September 1, 2017

Subject: Whether a Letcher County Ordinance enacting a business licensing tax upon businesses engaged in extracting non-renewable resources in Letcher County is lawful; whether a similar ordinance that was drafted to mirror the state severance tax would satisfy constitutional requirements.

Requested by: Woody Holbrook, Magistrate of District 3 of Letcher County

Written by: Taylor Payne, Assistant Attorney General

Syllabus: The business licensing tax must be fairly and equitably integrated with the county's general occupational or license tax, and therefore, not discriminatory as to the business of extracting non-renewable resources; the classification of these businesses for taxing must have reasonable basis; and taxing the businesses per operation must be rationally related to the business, rather than arbitrary or confiscatory. Because Letcher County does not have a general occupational tax, it has no authority to impose a tax only on the occupation of extracting non-renewable resources, because the tax would not be fairly and equitably integrated with a general occupational or license tax.

Statutes construed: KY CONST. § 171; KRS 143A.020

OAGs cited: OAG 17-003; OAG 79-385; OAG 79-301; OAG 82-543

Woody Holbrook, Magistrate for District 3 of Letcher County, Kentucky, has provided this office with a proposed Letcher County Ordinance enacting a business licensing tax upon businesses engaging in extracting non-renewable resources in Letcher County, Kentucky and has requested our opinion as to the legality of the Ordinance. We previously addressed the Letcher County Fiscal Court's authority to impose a license tax for the privilege of locating oil and gas wells upon request by Jamie Hatton, Letcher County Attorney, and direct your attention to that opinion, OAG 17-003, which is attached hereto. Therein, we advised that a license or occupational tax is constitutional if it is fairly and equitably integrated with a general county occupational or license tax; based upon reasonable classifications; uniform as to the class; and not discriminatory, arbitrary or confiscatory. *See* OAG 17-003 (citing OAG 79-385). Mr. Holbrook has also requested guidance as to whether a similar ordinance drafted to mirror the state severance tax would satisfy the requirements of the law. As to that issue, we advise that such an ordinance would still likely be found to be discriminatory as to the business of extracting non-renewable resources

A legislative body may create classes "'for the purpose of municipal licensing . . . and selection by a municipality among avocations, occupations and activities for raising revenue by license is allowed, providing the selection involves no unreasonable classification.'" *City of Lexington v. Motel Developers, Inc.*, 465 S.W.2d 253, 257 (Ky. 1971) (quoting McQuillin, *Municipal Corporations*, Third Edition, page 146, section 26.60). To that end, "differences in organization, management, and type of business may be sufficiently substantial to justify classification." *Id.* (citation omitted). Yet, "discrimination which does not have a reasonable basis is obviously arbitrary and violates the principle of equality and uniformity set forth in [S]ection 171." *Id.* (citation omitted). Practically speaking, the fiscal court may "not, without some rational basis, select a certain type of business enterprise and levy upon it a substantially heavier tax than that imposed upon other businesses which fall within the same general classification." *Id.*

In *Motel Developers*, the Court held a room tax imposed on hotels and motels by the City of Lexington as unconstitutional. *Id.* at 258. In Lexington, all businesses were taxed 1 and 1/2% of net profit, but hotels and motels were charged an additional 5% of the rent for occupancy of a room. *Id.* at 254. The

court reasoned this was a discriminatory tax because it amounted to the singling out of a particular business to carry out a proportionately heavier tax load than other businesses without any reasonable basis for creating such a classification. *Id.* at 258. In other words, the tax was not fairly and equitably integrated with the general occupational tax.

If a reasonable basis supports the taxing of a specific class of business, Section 171 of the Kentucky Constitution requires that "[t]axes shall be levied and collected for public purposes only and *shall be uniform upon all property of the same class* subject to taxation within the territorial limits of the authority levying the tax." (emphasis added). In Kentucky, courts have held this uniformity provision to be applicable to license taxes. *See Id.* at 256-57; *City of Louisville v. Aetna Fire Ins. Co.*, 143 S.W.2d 1074, 1075-76 (Ky. 1940). In *Paducah Automotive Trades Ass'n v. City of Paducah*, 211 S.W.2d 660, 665 (Ky. 1948), the Court stated when a license tax is imposed upon a class of persons engaged in a particular business, all persons engaged in such business are subject to the tax because the tax must be uniform on the class singled out for taxation. (citation omitted). In OAG 79-301, this office addressed the legality of a county occupational license tax on fire and casualty insurance companies. Applying Section 171 of the Kentucky Constitution, we advised that, "[s]uch a license tax must be uniform on all such insurance business in the county regardless of coverage." OAG 79-301.

In *Great Atl. & Pac. Tea Co. v. Kentucky Tax Comm'n*, 128 S.W.2d 581, 582 (Ky. 1939), the Court addressed a license tax imposed by the General Assembly on retail merchants that graduated according to the number of stores operated in the state. The Court framed the issue as to whether the "classification of merchants into groups based on the number of stores operated for the purpose of taxation is arbitrary and unreasonable." *Id.* at 585. The Court noted that, "[p]ersons engaged in the same occupation may be classified and a different license tax imposed upon each class, provided the classification is made upon a natural and reasonable basis." *Id.* (citations omitted). The Court concluded that the license tax bore no relationship to the volume of business, the abundance of capital of the business, the quantity of buying, buying for cash and skill in buying, but was arbitrarily fixed in accordance to the number of stores. *Id.* at 586 and 588. Such advantages, the Court concluded, are not peculiar to the ownership of multiple retail stores. *Id.* at 588. Thus, the Court held the difference in classifica-

tion for taxing purposes was in detail, rather than substance, and thus arbitrary and unconstitutional. *Id.* at 589.

Relying on our previous opinion, OAG 17-003, we advise that the Letcher County Fiscal Court may raise revenue by imposing a license of occupational tax on the business of extracting non-renewable resources. However, the tax must be fairly and equitably integrated with the county's general occupational or license tax, and therefore, not discriminatory as to the business of extracting non-renewable resources; the classification of these businesses for taxing must have a reasonable basis; and taxing the businesses per operation must be rationally related to the business, rather than arbitrary or confiscatory. Upon a request for input, Mr. Hatton informed this office that Letcher County currently does not have an occupational tax. Since Letcher County does not have an occupational tax in effect, the Letcher County Fiscal Court could not impose an occupational license tax upon businesses engaging in extracting non-renewable resources, because such a tax would not be fairly and equitably integrated with a general occupational tax in Letcher County. *See* OAG 82-543 (holding that Pulaski County could not impose an occupational license tax on itinerant businesses since the county did not have in effect an occupational license tax).

With respect to the issue of a similar ordinance drafted to mirror the state severance tax, we advise that such an ordinance enacted under the circumstances addressed above would still not be fairly and integrated with the county's general occupational or license tax, and therefore, likely found to be discriminatory as to the business of extracting non-renewable resources. KRS 143A.020(1) levies a tax for the privilege of severing or processing natural resources in the state at the rate of 4 and 1/2% on the gross value of the severed or processed. It applies to all taxpayers severing and/or processing natural resources in the state, and is in addition to other taxes. KRS 143A.020(2). Even if the ordinance at issue were drafted similarly to KRS 143A.020, the ordinance would still not be fairly and equitably integrated with a general occupational tax because no general occupational tax exists in Letcher County. As a result, the ordinance would still likely be unconstitutional because it discriminates against the business of extracting non-renewable resources.

ANDY BESHEAR

ATTORNEY GENERAL

A handwritten signature in cursive script, appearing to read "Taylor Payne".

Taylor Payne

Assistant Attorney General

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